

Bath & North East Somerset Council		
MEETING:	AVON PENSION FUND INVESTMENT PANEL	
MEETING DATE:	20 NOVEMBER 2019	AGENDA ITEM NUMBER
TITLE:	Review of Investment Performance for Periods Ending 30 September 2019	
WARD:	ALL	
AN OPEN PUBLIC ITEM		
<p>List of attachments to this report:</p> <p>Appendix 1 – Fund Valuation</p> <p>Appendix 2 – Mercer Performance Monitoring Report</p> <p>Exempt Appendix 3 – RAG Monitoring Summary Report</p> <p>Exempt Appendix 4 - Risk Management Framework Quarterly Monitoring Report (TO FOLLOW)</p> <p>Appendix 5 – Brunel Quarterly Performance Report</p> <p>Appendix 6 – Audit Log of Strategic Investment Decisions</p>		

1 THE ISSUE

- 1.1 This paper reports on the performance of the Fund's investment managers and seeks to update the Panel on routine aspects of the Fund's investments. The report contains performance statistics for period ending 30 September 2019.
- 1.2 The report focuses on the performance of the individual investment managers and the implementation of the investment strategy. The full performance report with aggregate investment and funding analysis will be reported to the Committee meeting on 6 December 2019.
- 1.3 The report also includes the Risk Monitoring report (exempt Appendix 4) produced by Mercer which includes details of the Fund's liability driven investment strategy and equity protection strategy. Due to the timing of publication of data in respect of these strategies the risk monitoring paper is marked to follow.
- 1.4 Appendix 5 is the quarterly performance report published by Brunel which focuses on the performance of the Brunel portfolios and responsible investment activity undertaken on the Fund's behalf over the quarter. Each Brunel portfolio review includes a dedicated ESG report which includes carbon foot-printing data, an 'insight' score which indicates current sentiment toward a company based on publically available information and a 'momentum' score which indicates the direction of travel of the company's 'insight' score over a 12 month period, designed to help investors assess whether a company is improving or deteriorating with respect to ESG factors. These metrics are used to derive a weighted average ESG score for each portfolio the Fund is invested in.

1.5 Appendix 6 is for reference only; it shows the implementation of strategic decisions following the 2017 Strategic Review and will be updated to reflect any strategic changes as they are made.

2 RECOMMENDATION

That the Panel:

2.1 Notes information as set out in the reports.

2.2 Identifies any issues to be notified to the Committee.

3 FINANCIAL IMPLICATIONS

3.1 The returns achieved by the Fund for the three years commencing 1 April 2019 will impact the next triennial valuation which will be calculated as at 31 March 2022. The returns quoted are net of investment management fees.

4 INVESTMENTS UPDATE

A – Fund Performance

4.1 The Fund's assets increased by £46m in the quarter ending 30 September 2019 giving a value for the investment Fund of £4,992m. Appendix 1 provides a breakdown of the Fund valuation and allocation of monies by asset class and managers.

4.2 Global equity markets ended the quarter in positive territory. Developed markets increased c.1.7% over the quarter while emerging markets declined. US and UK equities were up by 1.6% and 0.7% respectively. UK 10-year gilt yields fell 0.35% over the quarter and ended the quarter at 0.49%. The Fund's strongest performance came from the corporate bond and global equity managers. The Fund's infrastructure and multi-asset credit mandates posted positive returns as did the DGF's and property funds. Sterling weakened against the US Dollar and the Yen by 3.2% and 2.9% respectively and strengthened against the Euro by 1.1%. The net effect meant the currency hedge detracted c.0.5% from total Fund returns.

4.3 The Fund's overall performance relative to benchmarks is unavailable at the time of publishing. Full performance data will be reported to the Pensions Committee on 6 December 2019.

B – Investment Manager Performance

4.4 A detailed report on the performance of each investment manager has been produced by Mercer – see pages 22 to 41 of Appendix 2.

4.5 Brunel now reports on the performance of the assets they manage on behalf of the Fund. The report for each Brunel portfolio can be found in Appendix 5. However, Mercer will continue to provide quarterly commentary and analysis of all the Fund's mandates and at the strategic total fund level.

4.6 Manager absolute returns over the quarter were largely positive, with global equities, corporate bonds, real assets, credit and DGFs posting positive absolute returns. On a relative basis, active manager returns were mixed. One emerging market mandate significantly outperformed its benchmark while the Fund's global active equity mandate lagged. Over the 12 months to 30 September the majority of managers posted positive absolute returns but struggled to outperform on a relative basis. This was also true of 3 year returns, where the majority of managers

posted positive absolute returns but failed to keep pace with their respective benchmark with the exception of infrastructure which exceeded its cash benchmark by c.9%.

- 4.7 Exempt Appendix 3 summarises the latest internal report used by officers to monitor manager performance. The summary report highlights the managers that are rated amber or red, detailing the performance and/or organisational issue(s), how they are being monitored and any actions taken by Officers and/or the Panel.

C – Risk Management Framework Quarterly Monitoring Report

- 4.8 A detailed report of the performance of the Fund's risk management strategies including details of how the Fund's collateral position changed over the quarter is presented in Exempt Appendix 4. The full report is unavailable at time of publishing and will follow in due course.

5 INVESTMENT STRATEGY AND PORTFOLIO REBALANCING

- 5.1 **Asset Class Returns versus Strategic Assumptions:** Developed market equity returns over the last 3 years were 12.6% p.a., ahead of the assumed strategic return of 8.1% p.a. on the same basis. The 3 year return from emerging market equities was 8.4%; below the assumed 3 year return of 8.7%. Over the three-year period index-linked gilts returned 5.3% p.a. versus an assumed return of 2.2%. Similarly, property and infrastructure are ahead of their assumed strategic returns on a 3 year basis. Hedge fund returns remain below long-term averages and the strategic return of 5.1% p.a.

- 5.2 **Rebalancing:** There was no rebalancing activity during the quarter.

- 5.3 **Private Markets Investments:** The Fund has an allocation of 7.5% to Secured Income which is managed by Brunel. The drawdown of the committed capital started in Jan 2019. During 3Q19 a further commitment was made to a UK operating infrastructure equity fund which focuses on renewable energy assets. Investment into UK operating infrastructure is considered complimentary to traditional long-lease assets and serves to reduce the time taken to deploy capital (long investor queues remain in traditional long-lease funds) and also dampens sensitivity to the UK property market while not fundamentally altering the return profile of these predominantly inflationary-linked, income based investments. Separately, capital calls totalling £8.6m were issued by Brunel's underlying renewable infrastructure managers over the quarter. The Fund has now invested c.17% (£19.5m) of its total 2.5% (£115m) commitment to renewable infrastructure.

- 5.4 **Responsible Investment (RI) Activity:** The Fund signed the Global Investor Statement to Governments on Climate Change. The statement is a call from investors to policy makers for the urgent implementation of the Paris Agreement, a quicker transition to a low carbon economy and greater climate-related financial reporting. It has been signed by 515 investors managing over \$35 trillion in assets, including Brunel. Over the quarter, Brunel signed the investor statement on deforestation and forest fires in the Amazon, which has to date been endorsed by 244 investors representing approximately \$17.2 trillion in assets. The statement urgently requests companies to redouble their efforts and demonstrate clear commitment to eliminating deforestation within their operations and supply chains. Hermes - Brunel's appointed voting and engagement provider – also supported the investor statement. Appendix 5 includes details of the work being undertaken by Brunel as an active member of the PRI Plastic Working Group and presents the key findings of the most recent Transition Pathway Initiative Report on the Energy sector.

5.5 Voting and Engagement Activity: Hermes engaged with 25 companies held by Avon in the Brunel segregated portfolios on a range of 68 ESG issues. Environmental topics featured in 36.8% of engagements, 40% of which related directly to climate change. Social topics featured in 14.7% of engagements, where human capital management and corporate conduct and culture featured prominently. Of the 33.8% of Governance related engagements the majority of discussions revolved around executive remuneration. Aggregate voting data across all of the Fund’s investment managers will be reported to Committee at their next meeting. Post quarter end, Brunel supported a shareholder resolution calling on BHP Group to withdraw from industry groups with positions contrary to the Paris Agreement. Avon holds BHP Group in the Brunel UK active equity portfolio. The resolution won 27.1% support and despite not being carried has led to further engagement between company management and shareholders, which will inform BHP’s 2019 Industry Association Review.

6 RISK MANAGEMENT

6.1 The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

7 CLIMATE CHANGE

7.1 The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint. The Fund acknowledges the financial risk to its assets from climate change and is in the process of addressing this through its strategic asset allocation to Low Carbon Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee.

8 OTHER OPTIONS CONSIDERED

8.1 None.

9 CONSULTATION

9.1 The Council's Section 151 Officer has had the opportunity to input to this report and have cleared it for publication.

Contact person	Nathan Rollinson, Assistant Investments Manager (Tel: 01225 395357)
Background papers	Data supplied by Mercer, Brunel & State Street Performance Measurement
Please contact the report author if you need to access this report in an alternative format	